



STATE BOARD OF EQUALIZATION
PROPERTY AND SPECIAL TAXES DEPARTMENT
450 N STREET, SACRAMENTO, CALIFORNIA
PO BOX 942879, SACRAMENTO, CALIFORNIA 94279-0064
916 445-4982 • FAX 916 323-8765
www.boe.ca.gov

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April 13, 2005

TO INTERESTED PARTIES:

GUIDELINES FOR THE ASSESSMENT OF HISTORICAL PROPERTY

In Letter To Assessors 2005/020, the Board mailed proposed guidelines for the assessment of historical property enforceably restricted by contract. Interested parties were invited to provide comments on the proposed guidelines. Enclosed is a matrix summarizing the comments received.

An interested parties meeting will be held on April 25, 2005 to discuss the comments submitted on the proposed guidelines. The meeting will begin at 9:30 a.m. at the Board's headquarters in Sacramento, 450 N Street, Room 122. The guidelines are scheduled for discussion before the Property Tax Committee at the May 24, 2005 meeting.

All documents regarding this project will be posted to the Board's Web site at www.boe.ca.gov/proptaxes/histprop05.htm. If you plan to attend the interested parties meeting on April 25, please advise Ms. Glenna Schultz at glenna.schultz@boe.ca.gov or 916-324-5836.

Sincerely,

/s/ Dean R. Kinnee

Dean R. Kinnee, Chief
Assessment Policy and Standards Division

DRK:grs
Enclosure

ALTERNATIVE LANGUAGE

No.	PAGE/LINE REFERENCE	SOURCE	PROPOSED LANGUAGE	SBE STAFF POSITION
1	3-4	32-38, 1-12	<p>Orange County Assessor's Office</p> <p>Revise paragraph: Comparable rental data for single-family residences can be obtained from real estate brokers, rental agencies, and newspaper ads. Many assessors offices maintain rental data for commercial properties, and this data may be helpful when establishing the fair rent for restricted historical property when the contract allows a commercial use. Rental data for commercial property also can be obtained from commercial real estate brokers. <u>For the purposes of estimating anticipated market fair rent and expenditures for use in calculating the subject property's value, Actual</u> rental and expense data for existing restricted historical properties, <u>including the subject historical property</u>, can be obtained through an annual questionnaire sent to property owners.</p> <p>Revise paragraph: Allowed expenditures. Section 439.2(a)(3) defines allowed expenditures, or allowed expenses, to include expenses ordinary and necessary for the maintenance of the property's income. Typical expenses include insurance, utilities, repairs, and management fees. Expenses also may include amounts owing for special assessments or special taxes. Expenses that are not ordinary and necessary for the maintenance of the property's income should not be deducted. Such expenses include debt service, general property taxes, depletion, and interest on funds invested. As stated above, in general, allowed expenses are consistent with those allowed under Property Tax Rule 8(c). <u>For single-family residences, that are owner-occupied and not income producing, allowed expenditures shall not include actual expenses. The appraiser may instead use a percentage ratio derived from a market analysis and apply it against the imputed gross income.</u></p> <p>SBE REWRITE: Replace page 4, line 5 through line 12, with the following paragraphs: <u>Allowed expenses. Section 439(a)(3) defines allowed expenses, or allowed expenditures, as ordinary and necessary expenses necessary for the maintenance of the property's income. Allowed expenses are the same as those permitted in Property Tax Rule 8(c).</u> <u>Typical expenses include the cost of utilities, maintenance and repair, insurance, and property management. Allowed expenses also may include amounts owing for special assessments and special taxes. Expenses related to debt service, general property taxes, and depreciation should not be deducted.</u></p>	<p>Accepted.</p> <p>Not accepted – See rewrite.</p>

NO.	PAGE/LINE REFERENCE		SOURCE	PROPOSED LANGUAGE	SBE STAFF POSITION
1	3-4	32-38, 1-12	Orange County Assessor's Office	<p><u>In general, to arrive at the net income to be capitalized, allowed expenses are subtracted from the estimated rental income. However, in order to properly process the income, the appraiser must be aware of the structure of the lease with regard to how expenses are shared between the landlord-owner and the tenant.</u></p> <p><u>The proper perspective from which to view the processing of income and expenses is that of the landlord-owner. The objective is to estimate the net income to the landlord-owner—this is the amount that should be capitalized—and the correct question to ask is the following: What, if any, allowed expenses must the landlord-owner pay out of the rental income that he or she receives?</u></p> <p><u>In a gross lease, almost all of the allowed expenses must be paid out of the gross rent and therefore must be subtracted from the gross rent to arrive at the net income to be capitalized. In a net lease, relatively few allowed expenses must be paid by the landlord-owner out of the net rent (because the tenant pays most expenses) and only these expenses should be subtracted from the net rent to arrive at the net income to be capitalized. Frequently, there is a hybrid arrangement—some expenses are paid by the landlord-owner and some by the tenant. How expenses are shared often depends upon the property type together with local conventions.</u></p>	
2	4	34-36	Los Angeles County Assessor's Office	<p>The example contains an improvement with a remaining economic life (REL) of 20 years, resulting in an amortization component of five (5) percent (1/20). Without further explanation, the guideline in the letter implies that this component could be applied to the entire real property, including land and improvements. This appears to be incorrect, since the value component of the property related to the land should <i>not</i> reflect amortization. The current practice of Los Angeles County is to determine what percent the structure comprises of the total value, which if it were 65 percent would result in an amortization component of .0325 (.65 x .05). The same structure with an REL of 50 years would indicate a two (2) percent (1/50) amortization rate and subsequently an amortization component of .0130 (.65 x .02). Needless to say, this would also comport to universally accepted standard appraisal practice.</p> <p>SBE REWRITE: Add the following paragraph immediately after page 5, line 11: <u>Staff recognizes that under generally accepted appraisal principles, land is not a wasting asset and that an amortization component is typically not applicable to land income. However, the valuation method described in section 439.2 is by design formulaic and artificial in that its objective is to estimate a prescribed restricted value, not market value. Further, the language of the statute is clear and unambiguous. For these reasons, staff has chosen to simply follow the bare language of the statute with respect to income capitalization technique.</u></p>	Not accepted – See rewrite.

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3	EX		Tuolumne County Assessor's Office	Shouldn't there be a separate valuation of land? The way Tuolumne County does it is to try to estimate the income attributable to the land, without the amortization rate component and deduct that from the Net Operating Income. Then capitalize that remaining income using the capitalization rate, as in your example, with the amortization rate component to arrive at the value of the improvements. The total restricted value would then be the sum of the restricted land and restricted improvement values.	Not accepted. See response to #2.
4	6	27	San Diego County Assessor's Office	<p>Revise sentence: A review of the contract and other documents filed with the local planning department may help the appraiser determine whether any new construction to the existing structure is subject to the historical property contract and therefore subject to the provisions of section 439.2. Improvements existing as of the date of the contract would be subject to the provisions of section 439.2 unless specifically excluded by the contract. Any new construction made after the issuing date of the contract would not be subject to the provisions of section 439.2 unless specially included by an amendment to the contract.</p> <p>SBE REWRITE: Add sentence: <u>Any questions regarding new construction to enforceably restricted historical structures should be directed to the counsel of the legislative body of the city, county, or city and county who contracted with the property owner.</u></p>	Accepted.
5	7	6	Los Angeles County Assessor's Office	Pursuant to <i>City and County of San Francisco v. County of San Mateo</i> (10 Cal.4th 554), Mills Act properties are subject to the limitations of Article XIII A and thus are subject to supplemental assessments.	Not accepted. BOE previously decided that properties assessed under article XIII are not subject to supplemental assessment.
6	EX 1		Orange County Assessor's Office	<p>When valuing a single-family residence historical property or a mixed use or mixed valuation historical property that includes a single-family residence, the "anticipated operating expenses" should not include grounds maintenance, or water and garbage expenses. These are expenses typically paid by the renter/lessee/tenant of a single-family residence.</p> <p>SBE REWRITE: Add the following to Page 9, Line 28: <u>In each of the following examples, the gross income, or fair rent, is estimated on a gross rent basis, that is, under the assumption that the landlord-owner pays all operating expenses out of the gross income.</u></p>	Not accepted—see rewrite.

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7	EX 1, 3, 4		Orange County Assessor's Office	The Guidelines should state that the Homeowners' Exemption is not available to "restricted historical properties." Government Code section 50280.1 provides that "'Qualified historical property' for purposes of this article means privately owned property which is not exempt from property taxation..." Applying the homeowners exemption to a property will disqualify that property for historical property valuation. The homeowners' exemption deduction should not be included in Examples 1, 3, and 4.	Not accepted. AB 2104 (Ch. 965, Stats. 1985), which added § 50280.1 to the Revenue and Taxation Code, implemented recommendations made by the California Heritage Task Force. This report focused on the exemption under Rev. & Tax. § 214 (welfare exemption). The homeowners' exemption is not mentioned in the Task Force report or in any of the bill analyses for AB 2104.